

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

CHANGES CONCERNING
ATTRIBUTABLE COSTING

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Docket No. RM2016-13

**COMMENTS OF
AMAZON FULFILLMENT SERVICES, INC.**

(October 17, 2016)

Amazon Fulfillment Services, Inc. (“AFSI”) respectfully submits these comments on Order No. 3507 (issued September 9, 2016) (published at 81 Fed. Reg. 63445 (Sept. 15, 2016)). In Order No. 3507, the Commission proposes to revise 39 C.F.R. §§ 3015.7, 3060.10 and 3060.21 to conform to Order No. 3506, the Commission’s final decision in Docket No. RM2016-2, *Periodic Reporting (UPS Proposals One, Two, and Three)*. In Order No. 3506, the Commission changed its definition of attributable costs under 39 U.S.C. § 3622(c)(2), 3631(b) and 3633(a)(2) from the sum of volume-variable costs and product-specific costs to the incremental costs of each product. Order No. 3506 (Sept. 9, 2016) at 61-62, 123-24.

The proposed conforming changes do not raise any substantive issues left unresolved by Order No. 3506 itself, and thus should be adopted for the reasons explained in Order No. 3506. AFSI requests, however, that the Commission clarify the proposed rules and the regulatory preambles in Order No. 3507 in three limited respects.

(1)

First, on page 4 of Order No. 3507 (81 Fed. Reg. at 63446 col. 2), the Commission states that, while it “found that inframarginal costs are causally related to products, it

determined [that] inframarginal costs cannot be reliably identified, which is a necessary component of cost attribution. Order No. 3506 at 56.” To avoid confusion, this statement requires clarification.

The Commission is certainly correct that “inframarginal costs cannot be reliably identified,” Order No. 3506 at 56, because inframarginal costs cannot be computed without estimating fixed costs, and fixed costs can be estimated only by extending the total cost curve all the way to the origin (i.e., the point where the output of a cost driver is zero). The origin is far outside the relevant range of outputs observed in recent years. Hence, trying to infer the shape of the total cost curve and its intercept point on the vertical (cost) axis is no more than untestable guesswork. Order No. 3506 at 38-40.

As the Commission found in Order No. 3506, however, there is an independent and even more basic objection to the attribution of many inframarginal costs to individual products: the lack of any causal link between individual products and many inframarginal costs. Inframarginal costs in the *aggregate* are indeed causally related to the Postal Service’s aggregate output of *all* products, but only a minority of inframarginal costs are causally related to *individual* products. Hence, a large share of inframarginal costs could not be attributed to individual products *even if inframarginal costs could be identified and calculated reliably and with perfect accuracy*. Order No. 3506 at 31-32, 35, 45-51, 55.

(2)

Second, the Commission’s statement that inframarginal costs “are variable costs that do not vary *directly* with volume” (Order No. 3507 at 4) (emphasis in original) should also be clarified. What distinguishes inframarginal from marginal costs is not the directness or

indirectness of the relationship between volume and costs, but the absence of *any* causal relationship—either direct *or indirect*—between the level of the costs and the *marginal* (or last) unit of output of a product. Order No. 3506, App. A at 2-7. Hence, inframarginal costs are more accurately defined as variable costs that do not vary directly or indirectly with supplying the marginal, or last, unit of volume of a product. *See* Order No. 3506 at 35-36 and App. A at 16-17 (explaining concepts).¹

(3)

Third, proposed 39 C.F.R. § 3015.7(b) would define the attributable costs of each competitive product as follows:

Each competitive product must recover its attributable costs as defined in 39 U.S.C. 3631(b). Pursuant to 39 U.S.C. 3631(b), the Commission will use a competitive product's incremental costs, which is the sum of volume-variable costs, product-specific costs, and those inframarginal costs calculated as part of a competitive product's incremental costs, to calculate attributable costs.

The second sentence of this definition is circular: the phrase “incremental costs” appears as both the term to be defined and an element of the definition. The reference to “inframarginal costs” does not cure the circularity because the inframarginal costs of a product are calculated as the difference between its incremental costs and the sum of its volume-variable and product-specific fixed costs. Substituting the following language would cure the circularity:

¹ The statement that inframarginal costs “are variable costs that do not vary *directly* with volume” (Order No. 3507 at 4) might have been adopted from Order No. 3506 at 10 and 35, which in turn was a paraphrase of a statement by Dr. John Panzar. *Id.* at 35 (citing Panzar Decl. (Jan. 25, 2016), Exh. 2 at 11). The paraphrase, however, departed in a subtle but critical way from Dr. Panzar's actual formulation, which defined inframarginal costs as “variable costs that are not *volume variable* costs” (emphasis added)—i.e., are not *marginal* costs multiplied by volume. Panzar Decl. (Jan. 25, 2016), Exh. 2 at 11.

Each competitive product must recover its attributable costs as defined in 39 U.S.C. 3631(b). For this purpose, the costs attributed to each competitive product shall be the sum of its volume-variable costs, product-specific costs, and those inframarginal costs that the Postal Service incurs by supplying the entire output of the product and would avoid by not supplying the product (with all other outputs held constant).

See Order No. 3506, App. A at 7-12, 14-19 (explaining relationships between incremental, marginal and inframarginal costs). Adopting this definition would avoid needless confusion, and would allow the appropriate amount of inframarginal costs to be attributed to each product.

Respectfully submitted,

/s/

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